Supreme Court, U.S.
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No._____

In The
Supreme Court of the United States

RICHARD HARLEY & JAQUELINE KUBE,
Petitioners

vs.

SECURITIES AND EXCHANGE COMMISSION,
Respondent

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

PETITION FOR WRIT OF CERTIORARI

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QUESTIONS PRESENTED

1. Did the Circuit Court below improperly fail to reach the issue of whether the exclusionary rule applies in civil enforcement proceedings brought by the Securities and Exchange Commission?

2. Did the Circuit Court below misapply the doctrine of collateral estoppel?

3. Did the Circuit Court err in holding that the district court's finding of an independent source was not clearly erroneous.

LIST OF PARTIES

All parties appear in the caption of the case on the cover page.

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IN THE SUPREME COURT OF THE UNITED STATESPETITION FOR WRIT OF CERTIORARI

Petitioner respectfully prays that a writ of certiorari issue to review the judgment below.

OPINIONS BELOW

The *per curiam* opinion of the United States Court of Appeals for the Third Circuit appears at Appendix A to the petition and is unpublished.

The opinion of the United States District Court for the Middle District of Pennsylvania appears at Appendix B and is unpublished.

JURISDICTION

The date on which the United States Court of Appeals for the Third Circuit decided the case was September 30, 2008.

No petition for rehearing was timely filed in the case. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

United States Constitution, Amendment IV.

The right of people to be secure in their persons, houses, paper, and effects, against unreasonable searches and seizures, shall not be violated, and no warrants shall issue, but upon probable cause, supported by oath or affirmation, and particularly describing the place to be searched, and the persons or things to be seized.

United States Constitution, Amendment V.

No person shall be held to answer for a capital, or otherwise infamous crime, unless on a presentment or indictment of a grand jury, except in cases arising in the land or naval forces, or in the militia, when in actual service in time of war or public danger; nor shall any person be subject for the same offense to be twice put in jeopardy of life or limb; nor shall be compelled in any criminal case to be a witness against himself, nor be deprived of life, liberty, or property, without due process of law; nor shall private property be taken for public use, without just compensation.

STATEMENT OF THE CASE

This case arises pursuant to an order issued by the district court below that directed payment of disgorgement, prejudgment interest, and civil penalties. At all times pertinent, petitioners continuously asserted violations of their constitutional rights under the Fourth Amendment (illegal search and seizure) and the Fifth

Amendment (due process). The matter comes to this Court after several years of protracted litigation in the district and circuit courts.

In May 1996 the district court ordered a Permanent Injunction by Consent and Continued Asset Freeze and further ordered that the sole remaining issue would be whether the then defendants and relief defendant must disgorge funds, the amount of disgorgement, if any, and whether civil penalties, if any, should be assessed against them; and, should the parties be unable to agree on whether relief in the form of disgorgement or a civil penalty is appropriate, or as to the type, manner or amount of relief, such matters would be submitted to the district court for determination.

On January 23, 1997, the district court ordered the matter stayed pending the completion of parallel criminal proceedings. On March 13, 2006 the district court held the defendant/appellants in civil contempt for violation of its permanent injunction and continued asset freeze. On April 14, 2006 the defendant/appellants filed a motion to vacate that was denied by the district court on September 26, 2007.

On January 2, 2008 defendant/ appellants filed a motion to stay proceedings pending appeal. That motion was denied by the district court in

January 3, 2008. On January 4, 2008 the district court issued its final order directing payment of disgorgement, prejudgment interest, and civil penalties.

On January 25, 2008 the case was docketed in the United States Court of Appeals for the Third Circuit and, after briefing by the parties, the Circuit Court issued a non-precedential *per curiam* opinion affirming the judgment of the district court on September 30, 2008 and issued its mandate on November 21, 2008.

REASONS FOR GRANTING THE PETITION

The Court of Appeals for the Third Circuit has so far departed from the accepted and usual course of judicial proceedings as to call for an exercise of this Court's supervisory power; *i.e.,* the circuit court's flagrant disregard of the applicable standards in assessment of Petitioner's constitutional claims and its refusal to acknowledge the debatable nature of the district court's dispositive procedural ruling. The issues brought forward here will have a substantive impact on numerous individuals similarly situated

A. The Circuit Court Never Reached the Underlying Issue.

Here, the underlying constitutional rights

are; to be free from unreasonable search and seizure, and the denial of the right to due process.

On April 3, 1998 the district court ordered that defendant/appellants' motion to suppress evidence be granted and that "[a]ll evidence and fruits therefrom seized pursuant to the search warrant for defendants' personal residence, a premises known as North Slope 3, Unit 45A, Shawnee-On-Delaware, PA is suppressed." *See, Docket Entry #52*, Case #: 3:96-cr-00286. The district court continuously maintained that the aforementioned criminal case and the instant underlying civil action were "parallel" cases. Notwithstanding that order, the same court permitted the introduction of the previously suppressed evidence in the parallel civil action.

Justice Oliver Wendell Holmes put the issue succinctly in *Silverthorne Lumber Company v. United States,* 251 U.S. 385 (1920), when he stated that "[t]he essence of a provision forbidding the acquisition of evidence in a certain way is that not merely evidence so acquired shall not be used before the Court *but that it shall not be used at all*" (emphasis supplied) and "knowledge gained by the Government's own wrong cannot be used in the way proposed;" *accord, United States v. Wallace Tiernan Co. et al.,* 336 U.S. 793, 795 (1949) (citing "other cases in this Court have applied the same

rule;" *Weeks v. United States,* 232 U.S. 383; *Johnson v. United States,* 333 U.S. 10; *Go-Bart Co. v. United States,* 282 U.S. 344; *Byars v. United States,* 273 U.S. 28; *Gouled v. United States,* 255 U.S. 298; *United States v. Lefkowitz,* 285 U.S. 452; *Trupiano v. United States,* 334 U.S. *699; and cf. Harris v. United States,* 331 U.S. 145; *Zap* v. United States, 328 U.S. 624; *Davis v. United States,* 328 U.S. 582. *Id.* at fn 2.

In *Standard Oil Co. v. Iowa,* 408 F.2d 1171 (8th Cir. 1969), the Circuit Court cited the holding in *Lord v. Kelley,* 223 F. Supp. 684 (D, Mass) for the proposition that a suppression order is meant to prevent illegally obtained information:

"Looking to the factors considered in Lord v. Kelley, as weighing in favor of a limited suppression order, it is well to point out here that the government has tacitly admitted wrongdoing, that the illegal method of gaining access to the corporate records was unique and will not soon occur again, and that the defendants have vindicated the right to be free from misuse of statutes as a means of violating constitutional rights. A limited suppression order is far short of immunity but it is not a futile gesture.... In ruling on any discovery motions by the plaintiffs, the Court will take care to prevent, insofar as possible, the use of illegally obtained information." 281 F. Supp. 391, 410.

In *United States v. Sor-Lokken,* 557 F.2d 755, 758 the Tenth Circuit stated that: "It is well established that neither evidence seized during an unlawful search nor, as a general rule, evidence indirectly obtained as a result of such illegality is admissible against the victim of the search." *Wong Sun v. United States,* 371 U.S. 471 (1963); and that prejudice occurs when it is shown that some of the government's evidence would have been unknown to it, and thus unavailable. *Wong Sun* at 487-88; *United States v. Levy,* 577 F.2d 200 (3rd Cir. 1978); G*overnment of Virgin Islands v. Gereau,* 502 F.2d 914, 927-28 (3d Cir. 1974). "The exclusionary rule determines not only that illegally obtained evidence may not be directly presented to the court, but further that it may not be employed or relied on at all." However, "knowledge of these same facts gained from an independent source may still be employed" (*Sor-Lokken, supra,* citing *Silverthorne*).

Thus, in the instant case, the government could not use any information derived from the illegal search and seizure unless it had gained the information from an independent source. The government did not maintain that its case was established prior to the illegal search, admitted that it gained new knowledge that it did not already have, and that there was scant evidence of guilt independent of the illegal documents. *See, United States v. Dowler,* 978 F.2d 1268 (10th Cir. 1992).

Moreover, in the civil case the government made specific use of the illegally seized documents; the prosecution gained considerable comfort from reviewing all the records and was able to evaluate its case to ensure that it would not be surprised at trial – all to the eventual prejudice of petitioners.

As the district court stated, the criminal and civil cases ran "parallel" to each other. And there are inherent tensions between the purposes of civil discovery and the defendant's privilege against self-incrimination, or the potential for abuse of discovery (on both sides) by using discovery obtained in one proceeding in the other. *See, United States v. Michelle's Lounge,* 39 F.3d 684 (7th Cir. 1994).

B. The Circuit Court Relied on an Improper and Incorrect Application of the Doctrine of Collateral Estoppel.

The Circuit Court held that "[c]ollateral estoppel/issue bars *relitigation* (emphasis supplied) of a legal of factual issue when: '(1) the issue ... is the same as that involved in the prior action; (2) the issue was actually litigated, (3) it was determined by a final and valid judgment; and (4) the determination was essential to the prior judgment" (citing, *Peloro v. United States,* 488 F.3d 163, 175-75 (3d Cir. 2007)).

That is clearly the point. On January 29, 1998, petitioners moved to suppress the evidence seized from the search of the Harley/Kube residence, arguing that the search warrant for the residence was defective in that the supporting affidavit failed to establish probable cause for the search. The Government conceded that the affidavit presented to the magistrate judge failed to establish probable cause; as the Government explained, due to a clerical error in preparing the warrants, the supporting affidavit for the Lazare clinic was inadvertently duplicated and attached to both warrant applications, and the actual supporting affidavit for the residence was inadvertently omitted. On April 3, 1998, the district court granted the motion to suppress, stating that "the evidence obtained from defendants' personal residence ... will be suppressed."

Accordingly, the issue was actually litigated and it was determined by a valid and final judgment. Moreover, the issue in the civil action was clearly the same as that involved in the earlier criminal action and the determination was essential to the prior judgment. Therefore, all the criteria in *Pelero* were met and, if the doctrine of collateral estoppel were to be applied, it must be applied to operate as a bar against the government's argument; *i.e.*, since the district court had already ruled that the evidence must be suppressed in the

criminal case, the government must be collaterally estopped from using it in the subsequent civil action.

C. The Circuit Court Erred in Holding that the District Court's Finding of an Independent Source Was Not Clearly Erroneous.

In evaluating the finding by the district court, the Court of Appeals stated that "our review of the record confirms that the District Court's rejection of that argument was not clearly erroneous." But the panel never employed an adversarial testing process
to the argument that was advanced and gave no credibility to the fact that the alleged independent source, Ms. Loikits, could not have physically obtained the subscription agreements. Moreover, Loikitz was terminated in August but allegedly procured subscription agreement and other documents that were not created until October, November and December, but the Circuit Court never addressed that fact.

The SEC never provided either testimony or an affidavit from Lokitis; instead relying upon vague and contradictory affidavits from government agents. This was the sole "proof" that the SEC offered in the civil enforcement proceedings that they did, in fact, have an independent collateral source.

Defendant/Appellants challenged these assertions and provided a written timeline that clearly showed it would have been impossible for Lokitis to purloin the documents, as she said she did, because she never had physical access to the location where the documents were kept. What actually happened was that copies of the documents illegally seized in the criminal case were improperly given to the SEC by the Office of the U.S. Attorney. In addition, as demonstrated in their own memorandum, the Pennsylvania Securities Commission also requested copies of the relevant documents from the United States Attorney's office. To an objective fact finder, it was patently "more probable than not" that the SEC did not have and independent collateral source and the Circuit Court erred in holding that district court's finding was not clearly erroneous. It was clearly erroneous and prejudiced the petitioners.

CONCLUSION

WHEREFORE, for the foregoing reasons, the petition for a writ of certiorari should be granted.

Respectfully submitted,

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APPENDIX A

NOT PRECEDENTIAL

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

Nos. 07-4009 & 08-1127

SECURITIES AND EXCHANGE COMMISSION

v.

LAZARE INDUSTRIES, INC.;
RICHARD J. HARLEY; JACQUELINE KUBE

Richard J. Harley; Jacqueline Kube, Appellants

On Appeal from the United States District Court
for the Middle District of Pennsylvania
(D.C. Civil Action No. 96-cv-0705)
(Honorable Thomas I. Vanaskie)

Submitted Pursuant to Third Circuit LAR 34.1(a)
September 26, 2008

Before: SCIRICA, *Chief Judge*,
HARDIMAN and COWEN, *Circuit Judges*

(Filed: September 30, 2008)

OPINION OF THE COURT

PER CURIAM.

Richard J. Harley and Jacqueline Kube appeal *pro se* from the District Court's order entered September 26, 2007, and its final judgment entered January 4, 2008. For the following reasons, we will affirm the judgment of the District Court.

I.

Harley and Kube, husband and wife, owned and operated a company called Lazare Industries, Inc. ("Lazare"), through which they provided an "ozone/-oxygen enema" treatment to people suffering from HIV/AIDS and other medical conditions. From 1989 through 1996, Harley represented in various media that this treatment was a clinically-tested, patented procedure that neutralizes the virus that causes HIV/AIDS. On the basis of these representations, Harley sold unregistered shares of stock in Lazare. These sales were evidenced by stock subscription agreements, which are central to the issues on appeal. In 1996, the Securities and Exchange Commission ("SEC") instituted this civil enforcement action against Lazare, Harley and Kube, alleging, *inter alia,* that Harley's representations were knowingly false. Shortly after the SEC filed suit, defendants consented to a permanent injunction, which barred them from, *inter alia,* transferring assets during the pendency of the litigation.

Several months later, defendants were indicted on federal charges of mail fraud, wire fraud and

violations of the Federal Food, Drug and Cosmetic Act. The District Court stayed the civil action pending resolution of defendants' criminal charges, which ultimately resulted in convictions. During their criminal proceedings, defendants moved to suppress the subscription agreements on the grounds that they had been seized at their residence pursuant to a search warrant obtained by the Food and Drug Administration that the government conceded was defective. The District Court initially held the search illegal under the Fourth Amendment. At sentencing, however, the District Court allowed the government to use the subscription agreements to fix the appropriate amount of restitution after finding that the SEC had obtained them from an independent source – i.e., a former employee of Lazare named Dawn Loikits. The District Court sentenced Harley and Kube to terms of imprisonment and ordered Harley to pay restitution. We affirmed the criminal judgments. *See United States v. Harley,* C.A. Nos. 01-1823, 01-1916, 39 Fed. Appx. 789 (3d Cir. 2002). Defendants raised no issue regarding the subscription agreements on appeal.

The District Court then reopened the civil enforcement action. The SEC filed a motion to hold Harley and Kube in contempt for having transferred property in violation of the permanent injunction. After the District Court ordered them to show cause why they should not be held in contempt, defendants filed a motion to dismiss the order to show cause and the enforcement action itself, arguing that it was

premised on the allegedly illegally-obtained subscription agreements. The District Court denied that motion by order entered March 3, 2006. Defendants appealed, but their appeal was dismissed for failure to prosecute after they failed to pay the filing fee. *See SEC v. Lazare Indus., Inc.*, C.A. No. 06-1856 (Dec. 6, 2006). On March 13, 2006, the District Court held defendants in contempt of the permanent injunction. Defendants did not appeal that order. Instead, they filed a motion to vacate the permanent injunction and contempt order, once again arguing that they were impermissibly based on the subscription agreements. The District Court denied that motion by order entered September 26, 2007. Defendants' appeal from that order is pending as C.A. No. 07-4009.

Thereafter, the SEC filed a motion for a final judgment directing disgorgement and the payment of pre-judgment interest and civil penalties. The District Court held a hearing on the motion, at which the SEC used the subscription agreements to establish the amount of disgorgement. Defendants once again argued that the agreements should not be considered because they were illegally obtained, and the District Court once again rejected their argument. Following the hearing, the District Court entered its final judgment on January 4, 2008. The final judgment requires Harley and Kube to pay $975,911 in disgorgement and interest and imposes a $500,000

civil penalty on Harley. Defendants' appeal from that order is pending as C.A. No. 08-1127.[1]

II.

We have jurisdiction pursuant to 28 U.S.C. § 1291. On appeal, defendants raise no issue regarding the District Court's denial of their motion to vacate the permanent injunction and contempt order, and the only relief that they seek is the vacation of the final judgment. Accordingly, any potential issues that might relate solely to the order appealed from at C.A. 07-4009 are waived. Regarding the final judgment, defendants argue that the District Court erred in allowing the use of the subscription agreements because they were seized in violation of the Fourth Amendment and that the District Court held the SEC to too low a burden of proving that it had obtained the agreements from an independent source. Defendants also argue that the District Court abused its discretion in fixing the

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[1] The final judgment also imposes a $1,000,000 penalty on Lazare, and Harley and Kube purported to appeal on its behalf. By Clerk's order issued January 25, 2008 in C.A. No. 08-1127, they were notified that the appeal on behalf of Lazare would be dismissed unless an attorney entered an appearance on its behalf within 21 days. *See Simbraw, Inc. v. United States*, 367 F.2d 373, 374-75 (3d Cir. 1966); 3d Cir. LAR 107.2. No attorney has entered an appearance on behalf of Lazare. Accordingly, the appeal of Lazare is hereby dismissed.

amount of disgorgement and civil penalties. We reject these arguments.[2]

Defendants' first argument assumes that the exclusionary rule applies in civil enforcement proceedings brought by the SEC, which the SEC vigorously contests. We need not decide that issue. Even assuming that the exclusionary rule applies, defendants were collaterally estopped from relitigating the independent source issue in the civil proceeding and, in any event, the District Court's ruling on that issue was not clearly erroneous.

Collateral estoppel/issue preclusion bars relitigation of a legal or factual issue when: "(1) the issue . . . is the same as that involved in the prior action; (2) the issue was actually litigated; (3) it was determined by a final and valid judgment; and (4) the determination was essential to the prior judgment." *Peloro v. United States,* 488 F.3d 163, 174-75 (3d Cir. 2007) (citations omitted). At their criminal sentencing, defendants specifically argued that the government could not use the subscription agreements because it had not shown that it had obtained them from a source independent of the defective FDA

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[2] We review all legal issues *de novo,* but review for clear error the District Court's finding of an independent source, *see United States v. Provenzano,* 620 F.2d 985, 1005 (3d Cir. 1980), and for abuse of discretion its rulings on the amount of disgorgement, *see SEC v. Hughes Capital Corp.*, 124 F.3d 449, 455 (3d Cir. 1997), and civil penalties, *see SEC v. Sargent,* 329 F.3d 34, 38 (1st Cir. 2003).

search warrant. The District Court specifically rejected that argument after concluding that the government had presented sufficient evidence to demonstrate that the SEC had obtained the agreements from defendants' former employee, Ms. Loikits. (CA-00328.) That ruling was necessary to the criminal judgment because the use of the documents allowed the government to prove the appropriate amount of restitution. Accordingly, all the elements of collateral estoppel are present here. *See also United States v. Real Prop. Located in El Dorado County at 6380 Little Canyon Rd.*, 59 F.3d 974, 979-80 (9th Cir. 1995) (holding that defendant in a civil forfeiture action was collaterally estopped from relitigating Fourth Amendment issue previously litigated in a criminal action), *abrogation on other grounds recognized in United States v. $273,969.04 U.S. Currency*, 164 F.3d 462, 466 n.3 (9th Cir. 1999); *United States v. United States Currency in the Amount of $228,536.00*, 895 F.2d 908, 917-18, 921 (2d Cir. 1990) (same). Defendants did not base their challenge in the civil proceeding on any previously-unavailable evidence or legal authority, and there is no other equitable reason for declining to apply collateral estoppel in this case. *See National R.R. Passenger Corp. v. Pa. Pub. Util. Comm'n*, 288 F.3d 519, 525 n.3 (3d Cir. 2002) (discussing equitable exceptions to application of collateral estoppel).[3] Moreover, even if it were proper

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[3] Defendants argue that the District Court should have required the SEC to prove an independent source in the civil

(Continued on following page)

for defendants to relitigate this issue in the civil action, the District Court's finding of an independent source in that action was not clearly erroneous.[4]

Finally, defendants argue that the District Court (1) abused its discretion in fixing the amount of disgorgement because the SEC did not offer bank records showing that defendants actually received the amounts memorialized on the subscription agreements, (2) failed to consider relevant factors in fixing the amount of civil penalties, and (3) imposed civil penalties in excess of those authorized by 15 U.S.C. §§ 77t(d)(2)(C) and 78u(d)(3)(B)(iii). Each of these arguments lacks merit. Kevin DeLacy, an SEC staff accountant, testified at length at the January 4, 2008, hearing regarding how the subscription agreements

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proceeding by clear and convincing evidence and not merely by a preponderance of the evidence. Even in criminal cases, however, the government need only prove an independent source by a preponderance of the evidence. *See United States v. Pelullo*, 173 F.3d 131, 137-38 (3d Cir. 1999). Defendants have cited no authority suggesting that this burden is greater in *civil* cases. Thus, application of collateral estoppel is not precluded by any difference in the burden of proof.

[4] In particular, the District Court relied on (1) Ms. Loikits's testimony that she provided the subscription agreements to the SEC (CA-00547-49, 555, 558), and (2) a sworn declaration of John J. Heffernan, an SEC attorney and accountant, that Ms. Loikits delivered the subscription agreements to him (CA-00356-59). Defendants claim to have demonstrated that it would have been physically impossible for Ms. Loikits to have obtained the subscription agreements, but our review of the record confirms that the District Court's rejection of that argument was not clearly erroneous.

allowed him to reasonably approximate the amount of disgorgement. (CA-0071-79, CA-0086-103.) As for penalties, the statutes provide that the court shall determine the amount of penalties "in light of the facts and circumstances." 15 U.S.C. §§ 77t(d)(2), 78u(d)(3)(B)(i). They also provide for a maximum penalty of $100,000 for individuals for *each* violation (i.e., each of Harley's at least 54 sales of stock). *See id.* In imposing a penalty of $500,000 on Harley, the District Court specifically discussed the "egregious" nature of his fraud and noted, correctly, that it could have imposed a larger penalty than it did. (CCA-00113-14.) In sum, the District Court acted well within its discretion and did not otherwise err in determining the amounts of disgorgement and civil penalties.

Accordingly, we will affirm the judgment of the District Court.

APPENDIX B

IN THE UNITED STATES DISTRICT COURT FOR THE MIDDLE DISTRICT OF PENNSYLVANIA

SECURITIES AND EXCHANGE COMMISSION, Plaintiff, v. LAZARE INDUSTRIES, INC. and RICHARD HARLEY, Defendants, and JACQUELINE KUBE, Relief Defendant.	Case NO. 3:CV-96-0705 (Chief Judge Thomas I. Vanaskie)

FINAL JUDGMENT AND ORDER DIRECTING PAYMENT OF DISGORGEMENT, PREJUDGMENT INTEREST, AND CIVIL PENALTIES

(Filed Jan. 4, 2008)

WHEREAS, on May 20, 1996, this Court entered a Permanent Injunction by Consent and Continued Asset Freeze (the "Permanent Injunction"), reserving only the issue of whether the defendants and relief defendant must disgorge funds, the amount of disgorgement, if any, and whether civil penalties, if any should be assessed against the defendants;

AND WHEREAS NOW, the plaintiff, the Securities and Exchange Commission has moved this Court for an Order Directing Payment of Disgorgement, Prejudgment Interest, and Civil Penalties (the "Commission's Motion");

IT IS HEREBY ORDERED, ADJUDGED and DECREED THAT, on this 4th day of January, 2008, upon consideration of the Commission's Motion, and of all responses and replies to that Motion, and there being no just reason for delay, the plaintiff 's Motion is hereby **GRANTED** in full, and:

I.

IT IS HEREBY ORDERED, ADJUDGED, AND DECREED that that Defendants Lazare Industries, Inc. ("Lazare") and Richard J. Harley ("Harley"), and Relief Defendant Jacqueline Kube ("Kube") are jointly and severally liable for disgorgement of $442,000 [424,250] representing profits gained as a result of the conduct alleged in the Complaint in the captioned action, together with prejudgment interest thereon in the amount of ~~$574,742~~ [551,661] for a total of ~~$1,016,742~~ [975,911]. The Commission may enforce the Court's judgment for disgorgement and prejudgment interest by moving for civil contempt (and/or through other collection procedures authorized by law) at any time after ten (10) days following entry of this Final Judgment. Payments under this paragraph shall be made to the Clerk of this Court, together with a cover letter identifying the paying Defendant

as a defendant in this action; setting forth the title and civil action number of this action and the name of this Court; and specifying that payment is made pursuant to this Final Judgment. The paying Defendant shall simultaneously transmit photocopies of such payment and letter to the Commission's counsel in this action. By making this payment, the paying Defendant relinquishes all legal and equitable right, title, and interest in such funds, and no part of the funds shall be returned to any Defendant. The Clerk shall deposit the funds into an interest bearing account with the Court Registry Investment System ("CRIS") or any other type of interest bearing account that is utilized by the Court. These funds, together with any interest and income earned thereon (collectively, the "Fund"), shall be held in the interest bearing account until further order of the Court. In accordance with 28 U.S.C. § 1914 and the guidelines set by the Director of the Administrative Office of the United States Courts, the Clerk is directed, without further order of this Court, to deduct from the income earned on the money in the Fund a fee equal to ten percent of the income earned on the Fund. Such fee shall not exceed that authorized by the Judicial Conference of the United States. The Commission may propose a plan to distribute the Fund subject to the Court's approval. Defendant shall pay post-judgment interest on any delinquent amounts pursuant to 28 U.S.C. § 1961.

II.

IT IS FURTHER ORDERED, ADJUDGED, AND DECREED that, pursuant to Section 21(d)(3) of the Exchange Act [15 U.S.C. § 78u(d)] and Section 20(d) of the Securities Act [15 U.S.C. § 77t(d)], Defendant Harley shall pay a third-tier civil penalty in the amount of $500,000; and Defendant Lazare shall pay a third-tier civil penalty in the amount of $1,000,000. The Defendants shall make their respective payments within ten (10) business days after entry of this Final Judgment by certified check, bank cashier's check, or United States postal money order payable to the Securities and Exchange Commission. The payment shall be delivered or mailed to the Office of Financial Management, Securities and Exchange Commission, Operations Center, 6432 General Green Way, Mail Stop 0-3, Alexandria, Virginia 22312, and shall be accompanied by a letter identifying the paying Defendant as a defendant in this action; setting forth the title and civil action number of this action and the name of this Court; and specifying that payment is made pursuant to this Final Judgment. The Defendants shall pay post-judgment interest on any delinquent amounts pursuant to 28 U.S.C. § 1961. The Commission shall remit the funds paid pursuant to this paragraph to the United States Treasury.

III.

IT IS FURTHER ORDERED, ADJUDGED, AND DECREED that the permanent injunctions

imposed in paragraphs I. and II. of the Permanent Injunction shall remain in full force and effect; and

IV.

IT IS FURTHER ORDERED, ADJUDGED, AND DECREED that this Court shall retain jurisdiction of this matter for the purposes of enforcing the terms of this Order.

Dated: January 4, 2008

/s/ Thomas I. Vanaskie
The Honorable Thomas I. Vanaskie
Chief United States District Judge

APPENDIX C

IN THE UNITED STATES DISTRICT COURT FOR THE MIDDLE DISTRICT OF PENNSYLVANIA

SECURITIES AND EXCHANGE	:	
Plaintiff	:	
v.	:	
LAZARE INDUSTRIES, INC., and RICHARD J. HARLEY	:	**NO. 3:CV-96-0705**
	:	**(JUDGE VANASKIE)**
Defendants	:	
and	:	
JACQUELINE KUBE	:	
Relief Defendant	:	

ORDER

September 26, 2007

THE BACKGROUND OF THIS ORDER IS AS FOLLOWS:

On April 22, 1996, the Securities and Exchange Commission ("SEC") brought this action, alleging that Defendants Lazare Industries, Inc. ("Lazare") and Richard J. Harley had engaged in a scheme to defraud more than seventy investors by making fraudulent representations and omissions in connection with an offer and sale of more than $1 million of Lazare common stock. The Complaint further alleged that

relief defendant Jacqueline Kube had improperly converted investor funds for her personal use. The fraudulent scheme concerned defendant Harley's efforts to market ozone therapy by rectal insufflation and other means as a treatment modality for cancer, AIDS, and other serious maladies.

On April 25, 1996, this Court, acting *ex parte,* issued an Order temporarily freezing Defendants' assets, requiring that they account for investor funds, and establishing an expedited discovery schedule. On May 1, 1996, the SEC attempted to depose both Harley and Kube in preparation for a preliminary injunction hearing, but each invoked the Fifth Amendment privilege against self-incrimination.

On May 16, 1996, Harley, Kube, and Lazare, acting upon the advice of counsel, agreed to a "Permanent Injunction by Consent and Continued Asset Freeze." On May 20, 1996, the consent Order was issued. Among other things, the Order restrained Defendants from violating the federal securities laws, enjoined Defendants from seeking protection under the bankruptcy laws, and restrained Defendants from disposing, transferring, pledging, encumbering, assigning, dissipating, concealing, or otherwise disposing of any funds or assets. The Order further provided that "the sole remaining issue in this action shall be whether the defendants and relief defendant must disgorge funds, the amount of disgorgement, if any, and whether civil penalties, if any, should be assessed against the defendants." (Dkt. Entry 19 at 5.)

On November 12, 1996, a multi-count indictment was returned against Lazare, Harley and Kube, charging violations of criminal law for the same conduct that formed the predicate for this SEC civil enforcement action. As a consequence of the commencement of criminal proceedings, litigation in this action was stayed by Order entered on January 23, 1997.

The criminal proceedings were protracted. Defendants filed a number of motions, including a motion to suppress evidence seized from the personal residence occupied by Defendants Harley and Kube. The government conceded that it had erroneously attached to the search warrant application for the residence an affidavit that pertained to Defendants' business premises. In a Memorandum and Order entered on April 3, 1998, this Court concluded that the warrant issued for the search of the Harley/Kube residence was not supported by probable cause and that the good faith exception recognized in *United States v. Leon,* 468 U.S. 897 (1984), did not apply. Accordingly, the motion to suppress was granted.

Of course, the suppression ruling did not terminate the criminal prosecution. An evidentiary hearing was held on May 8, 1998, for the purpose of determining what evidence had not been derived from the search of the residence. The case proceeded to a jury trial in late May of 1998. After several days of deliberations, the jury reported that it was deadlocked, and a mistrial was declared. A second trial was held

in May of 2000, resulting in the convictions of Harley, Kube, and Lazare.

A sentencing hearing was conducted on March 30, 2001. Harley had objected to the calculation of loss, asserting that stock subscription agreements taken from his residence had been used to tabulate the amount. Based upon the evidence presented by the government at the sentencing hearing, this Court determined that the government had established an independent source for the stock subscription agreements used in the loss calculation. Specifically, the evidence showed that a disgruntled former employee and investor, Dawn Loikits, had provided the stock subscription agreements to an SEC staff attorney. (Transcript of March 30, 2001 Sentencing Hearing in *United States v. Harley,* 96-CR-286, at 19;[1] Declaration of John J. Heffernan, submitted as Exhibit "B" to the SEC brief in Opposition to Defendants' Motion to Vacate, Dkt. Entry 101-5.) Harley received a five year prison term, to be followed by a supervised release period of two years.

In August of 2002, the Court of Appeals for the Third Circuit affirmed the convictions and sentences of Harley and Kube. The Supreme Court denied Harley's petition for a writ of certiorari in February of 2003.

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[1] Excerpts of the sentencing transcript are included as Exhibit "A" to the SEC Brief in Opposition to Defendants' Motion to Vacate, Dkt. Entry 101-4.

The criminal proceedings having been completed, the SEC, in November of 2004, moved to lift the stay of litigation in this matter. In the brief supporting its motion, the SEC asserted that Defendants had transferred and encumbered property in violation of the Asset Freeze Order. (Brief in Support of Motion to Lift Stay, Dkt. Entry 70, at 5.) By Order dated September 26, 2005, this Court granted the Motion to Lift the Stay. (Dkt. Entry 74.)

On January 27, 2006, the SEC moved for an Order to show cause why Harley and Kube should not be held in contempt of the May 20, 1996 "Permanent Injunction by Consent and Continued Asset Freeze." (Dkt. Entry 79.) By Order dated February 3, 2006, Harley and Kube were directed to appear in Court to show cause why they should not be held in contempt for violating the May 20, 1996 Asset Freeze Order. (Dkt. Entry 84.) They were also directed to provide the SEC with a sworn accounting of all assets that were subject to the May 20, 1996 Asset Freeze Order. (*Id.*) Finally, the Order authorized expedited discovery. (*Id.*)

Harley and Kube failed to comply with the February 3, 2006 Order. Instead, on March 2, 2006, one day before the scheduled hearing date on the show cause order, they moved to dismiss this matter on the grounds that it rested upon evidence illegally seized from their residence. Concluding that Defendants could not collaterally challenge the validity of the Asset Freeze Order in a contempt proceeding

(Transcript of March 3, 2006 Hearing, Dkt. Entry 90, at 7-8), this Court denied the motion to dismiss.

By Order dated March 13, 2006, this Court found Harley and Kube in civil contempt of the Asset Freeze Order. To purge this contempt, Harley and Kube were directed to pay $108,000 plus prejudgment interest in the amount of $23,732 into the Registry of this Court. In addition, Harley and Kube were directed to make a full and complete sworn accounting of all assets that were ever subject to the May 20, 1996 Asset Freeze Order. Harley and Kube did not comply with the March 13, 2006 Order.

Instead, on April 14, 2006, they moved to vacate the 1996 Asset Freeze Order and the 2006 Civil Contempt Order. (Dkt. Entry 99). This motion was once again premised upon the assertion that the civil enforcement proceeding rested upon documents obtained as a result of the illegal search of their residence.[2]

Defendants argue that the Asset Freeze Order as well as the Civil Contempt Order must be set aside on the grounds that this Court lacked jurisdiction because the SEC civil enforcement proceeding rested upon illegally seized documents. Defendants' arguments are legally and factually fallacious.

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[2] Defendants also had appealed the denial of their motion to dismiss the show cause order. On December 6, 2006, the Court of Appeals for the Third Circuit dismissed the appeal due to Defendants failure to timely prosecute the matter.

Subject matter jurisdiction is a matter of congressional action. Exercise of subject matter jurisdiction is not dependant upon the source of evidence used by a party. In this case, there is no dispute that Congress has conferred subject matter jurisdiction on federal courts to entertain civil enforcement proceedings brought by the SEC. *See* 15 U.S.C. §77v; 15 U.S.C. §78aa. These statutes provide that District Courts have jurisdiction over all suits in equity and actions at law brought to enforce any liability or duty created by the Securities Act of 1933, 15 U.S.C. §§ 77a, *et seq.,* and the Securities Exchange Act of 1934, 15 U.S.C. §§ 78a, *et seq.,* respectively. Jurisdiction, *i.e.*, the authority to act, is not affected by the admissibility *vel non* of certain evidence.

In this case, Defendants, with the assistance of counsel, agreed to an Asset Freeze Order. That Order has remained in full force and effect since its entry in May of 1996. The suppression ruling upon which Defendants now rely was entered in April of 1998. Although a stay of litigation was then in effect, the Asset Freeze Order remained in place. If Defendants wanted to avoid the constraints of the Asset Freeze Order, they could have moved to lift the stay of litigation. In this regard, the stay order provided that it may be vacated upon good cause shown. Defendants did not seek to challenge the validity of the Asset Freeze Order, but did proceed to violate it. They acted at their peril in transferring and encumbering assets subject to an Order of this Court

Defendants may not collaterally challenge the validity of the order to which they assented. As stated in *Maggio v. Zeitz,* 333 U.S. 56, 69 (1948):

> It would be a disservice to the law if we were to depart from the long-standing rule that a contempt proceeding does not open to reconsideration the legal or factual basis of the order alleged to have been disobeyed and thus become a retrial of the original controversy. The procedure to enforce a court's order commanding or forbidding an act should not be so inconclusive as to foster experimentation with disobedience.

Simply stated, "the validity of [an] Order is not open to collateral attack in a contempt proceeding for violating it." *Harris v. City of Phila.,* 47 F.3d 1333, 1337 (3d Cir. 1995).

Defendants lament that they did not have knowledge of grounds upon which to contest the SEC's use of stock subscription agreements. That fact, however, is of no consequence. The pertinent fact is that they agreed to be bound by the Asset Freeze Order, and they cannot evade the effect of that Order by asserting that some evidence was later found to be excludable.

Indeed, it is doubtful that the exclusionary rule would even apply in this civil enforcement proceeding. In this regard, "the Supreme Court has never applied the exclusionary rule to exclude evidence from a civil proceeding, federal or state." *SEC. v. Tyler,* No. Civ. A. 3:02-CV-0282, 2002 WL 32538418, at

*7 (N.D. Tex. Feb. 21, 2002). In *United States v. Janis,* 428 U.S. 433 (1976) the Court declined to apply the exclusionary rule in a civil action to enforce federal tax laws. In *INS v. Lopez-Mendoza,* 468 U.S. 1032 (1984), the Court ruled that the exclusionary rule does not apply in civil deportation proceedings. In *Tyler,* the district court relied upon the absence of any Supreme Court precedent applying the exclusionary rule in civil proceedings to rule that an argument similar to that presented here – illegally seized evidence had been used by the SEC – did not undermine the SEC application for preliminary injunctive relief. Similarly, the argument advanced here does not undermine the action taken by the SEC to enforce a consent Order.

In any event, the SEC demonstrated an independent source for the stock subscription agreements. The affidavit of John J. Heffernan attests to the fact that he received the stock subscription agreements from Dawn E. Loikits, a former employee of Lazare. He further attests that the stock subscription agreements obtained from Ms. Loikits were attached as Exhibit G to the Declaration of Paul F. Boeggeman, which accompanied the SEC Motion for Temporary Restraining Order, Asset Freeze and Other Relief filed in this matter on April 22, 1996. Moreover, the SEC has pointed to testimony of Ms. Loikits given in the criminal proceeding on May 8, 1998, in which she testified that she took the Lazare stock subscription agreements and provided them to the SEC. (Exhibit "E" to the Brief in Opposition to the Motion to Vacate

Order, Transcript of May 8, 1998 Hearing at 172, Dkt. Entry. 101-8 at 173.) The SEC also makes the pertinent observation that this Court found that the documents submitted in support of the civil enforcement proceeding had a source independent of the illegal search of the Harley/Kube residence when those documents were used to calculate the loss sustained as a result of Defendants' fraud. The documents used to calculate the loss included the assailed stock subscription agreements.

It is therefore clear that there is neither a factual nor a legal basis for setting aside the Asset Freeze Order or the ensuing Contempt Order. **ACCORDINGLY, IT IS HEREBY ORDERED THAT** Defendants' Motion to Vacate (Dkt. Entry 99) is **DENIED**.

s/ Thomas I. Vanaskie
Thomas I. Vanaskie
United States District Judge